[2016] UKFTT 0177 (TC)

TC04963

Appeal number: TC/2015/02981

Value Added Tax – penalty for deliberate inaccuracies in VAT returns – schedule 24 Finance Act 2007 – whether appellant's behaviour was deliberate – held yes – appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

GRYSON AIR CONDITIONING EQUIPMENT LTD **Appellant**

- and -

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE & CUSTOMS **Respondents**

TRIBUNAL: JUDGE ROBIN VOS
MOHAMMED FAROOQ

Sitting in public at Centre City Tower, Birmingham on 26 February 2016

The Appellant did not attend and was not represented.

Mrs Helen Perrett, Tribunal caseworker, HM Revenue and Customs, for the Respondents

DECISION

Introduction

1. The Appellant, Gryson Air Conditioning Equipment Ltd is based in the Welsh valleys. It is a small company having two directors and, at the relevant time, employing ten employees. It supplies and installs air conditioning systems.

2. Following a compliance visit by HMRC on 19 February 2014, it was accepted that the appellant's VAT returns for the 06/11 – 06/13 periods were inaccurate in that it had understated the VAT payable by £214,289.

3. HMRC concluded that the inaccuracies were deliberate and imposed a penalty under schedule 24 to Finance Act 2007 ("FA 2007") of £86,251.30 representing 40.25% of the under declared tax.

4. The appellant appeals against the penalty on the basis that the inaccuracies were not deliberate.

Proceeding with the hearing in the appellant's absence

5. Neither of the appellant's directors, Mr Gareth Jones and Mr Chrys Agland attended the hearing and no representative of the appellant had been appointed.

6. On 25 February 2016, Mr Jones wrote an email to the Tribunal containing a short statement which he requested should be considered by the Tribunal. He wrote a further email on the morning of the hearing, 26 February 2016 confirming that he would be unable to attend the hearing but asking for confirmation that his statement sent the previous day had been received and that it would be seen by the Tribunal.

7. It is apparent from these emails that the appellant was aware of the hearing and expected it to proceed in its absence.

8. Mrs Perrett, representing HMRC confirmed that she had spoken to Mr Jones on 25 February 2016 shortly before he sent his email to the Tribunal. He explained to her that he was worried about attending the Tribunal and asked if it was compulsory for him to attend. Mrs Perrett explained that he was not obliged to attend but that he would lose the opportunity to put his case before the Tribunal in person.

9. We have reviewed the evidence which includes a number of letters and emails together with a statement from the directors of the appellant which, together, set out the appellant's case clearly and consistently.

10. Taking all of these factors into account, the Tribunal considered that it was in the interest of justice to proceed with the hearing in the absence of the appellant in accordance with all 33 of the Tribunal Procedure (First Tier Tribunal) (Tax Chamber) Rules 2009.

The evidence and the facts

11. The Tribunal had before it a number of bundles prepared by HMRC containing relevant correspondence and documents including a witness statement from Mrs Michelle Mansell, the VAT officer who conducted the enquiry leading to the imposition of the penalties as well as a witness statement from Gareth Jones and a further statement from the directors of the appellant. The Tribunal also heard oral evidence from Mrs Mansell.

12. Based on this evidence, the Tribunal finds the following facts.

13. Robert Newton, an officer at HMRC's local compliance, small and medium enterprises office in Cardiff conducted a compliance visit to the appellant on 6 May 2011. During that visit, the appellant made a voluntary disclosure of unpaid output tax totalling £31,799.06.

14. This discrepancy resulted from the appellant's book-keeper using manual records of sales invoices to prepare the VAT returns rather than using the information contained in the Sage accounting system. The manual records were incorrect which meant that some sales invoices appeared in VAT returns for later periods than should have been the case whilst other sales invoices were missed off the VAT returns completely.

15. The particular invoices which had been omitted related to the period from 31 October 2010 to 1 December 2010.

16. At some point between December 2010 and May 2011, a new book-keeper was appointed by the appellant. Mr Newton was satisfied by the end of his compliance visit that the new book-keeper understood the errors that had been made and had committed to rely on the Sage tax points as shown in the Sage day book reports in order to avoid future errors.

17. Despite this, the appellant continued to rely on manual schedules of sales invoices. All of the appellant's VAT returns for the 06/11 – 06/13 periods contained inaccuracies in relation to the sales figures. All of these inaccuracies were understatements of the amount of sales – i.e. they were in the appellant's favour. The figures for purchases/input tax in all of these VAT returns were however correct.

18. The inaccuracies consisted of the following:

    (1) Using sales figures for months which were not covered by the VAT return but instead were earlier months.

    (2) Showing only a part of the sales figures for some months.

    (3) Omitting the sales figures for some months in their entirety.

19. At some point between May 2011 and February 2014, the book-keeper who was in post at the time of the original compliance visit in May 2011 retired and was replaced by a new book-keeper, Valerie Williams.

20. Both book-keepers were under some pressure as a result of personal problems. Whilst she was working for the appellant, the first book-keeper's father died. Ms Williams' marriage of 32 years broke down. She lost her family home and her car and had to move into rented accommodation.

21. On 8 October 2013, HMRC's booking team telephoned the appellant to arrange a VAT assurance visit. They managed to speak to Mr Agland on 20 October 2013.

22. The VAT return for the period ended 09/13 was prepared by Mr Jones rather than the book-keeper. This return was found to be accurate.

23. Having been unable to arrange a date for the assurance visit and having not heard from the appellant since 20 November 2013, HMRC wrote to the appellant on 29 January 2014 informing it that Mrs Mansell would be conducting a visit on 19 February 2014.

24. At the start of that visit, which was attended by Mr Agland and Mr Jones, it was voluntarily disclosed by them that sales had been omitted from VAT returns prior to the 09/13 period. No calculation of the omitted sales was provided.

25. During the compliance visit, Mrs Mansell was given full access to the appellant's books and records in order to enable her to calculate the extent of the inaccuracies in the relevant VAT returns.

The penalty regime

26. Where a VAT return contains an inaccuracy which is careless or deliberate and that inaccuracy leads to an understatement of a liability to tax, HMRC is obliged by paragraph 1 of schedule 24 to FA 2007 to charge a penalty.

27. The amount of the penalty depends on whether the taxpayer's conduct is careless or deliberate, whether the inaccuracy is concealed and whether the disclosure was prompted.

28. It is not disputed in this case that the disclosure was prompted and that the inaccuracy was not concealed. The question is whether the appellant's behaviour was careless or deliberate.

29. If the inaccuracy is careless, the standard penalty is 30%. If it is deliberate, the standard penalty is 70%. In either case, the penalty can be reduced based on the taxpayer's level of disclosure and co-operation but it cannot be reduced below 15% for a careless inaccuracy or 35% for a deliberate inaccuracy (paragraphs 9 and 10 schedule 24 to FA 2007).

30. HMRC can apply a special reduction under paragraph 11 of schedule 24 to FA 2007 if there are "special circumstances". This does not however include an inability to pay.

31. If the inaccuracy is careless, HMRC has power to suspend the penalty subject to satisfaction by the taxpayer of certain conditions for a specified period of time. There is no power to suspend a penalty for a deliberate inaccuracy.

32. Based on the above, the main question for the Tribunal is whether the inaccuracies in the appellant's VAT returns were deliberate rather than careless. There is a supplementary question in either case as to whether HMRC's reduction of 85% for disclosure/co-operation is the right figure.

Were the inaccuracies deliberate

33. The appellant's case is straightforward. The directors say that they left the VAT returns to the book-keeper who had "full autonomy" during the relevant periods. The directors were very busy keeping the business going and are largely based onsite at various customers' premises throughout the UK.

34. The directors make the point that the book-keepers were under significant personal strain as a result of events taking place in their personal lives and that this may well be the reason why they made mistakes in the VAT returns.

35. Whilst acknowledging that they should perhaps have monitored the book-keepers more closely or checked the VAT returns more carefully, they say that they did not do so. Whilst they would look at the VAT returns, they would only look at the bottom line – i.e. how much VAT had to be paid and not at the rest of the summary of the VAT return. As a result, they have said that they did not notice the discrepancy in the sales figures and did not become aware of the inaccuracies until either September or November 2013 when they were alerted to it by their accountant.

36. The directors drew our attention to the fact that they are not book-keepers or qualified accountants or indeed IT experts. They are not office based and rely on the work of others to undertake the book-keeping and financial functions of the company.

37. A further point made by the directors is that they were well aware of the problem which was brought to light by the previous compliance visit from HMRC in May 2011. As a result of this, the directors sometimes went without salaries to enable suppliers and HMRC to be paid back. They were therefore hardly likely to deliberately allow the same mistakes to be made which would then result in further substantial under payments which would in due course have to be paid back. In their own words "we are not the type of businessmen that take their obligations lightly".

38. HMRC on the other hand takes a rather different view of matters. Mrs Perrett made the point that the amounts of understated VAT were very significant. In one quarter, for example (the VAT period ended 03/12), the underpaid VAT was £46,241.92. This equates to over £200,000 of sales for a business which, in the relevant period, had a quarterly turnover of less than £400,000. It is, she says, not credible that the directors who are running the business would not notice that the sales figures were understated by such a large amount.

39. Mrs Perrett also drew attention to the fact that the inaccuracies spanned a period of more than two years. This is in her view evidence that the inaccuracies cannot merely have been careless mistakes but were part of a deliberate pattern of under-declaration.

40. She submitted that this is reinforced by the knowledge that, during the previous visit in May 2011, Mr Newton made sure that the book-keeper understood what had been going wrong and how to put it right. Yet, despite this, every VAT return after that visit contained the same inaccuracies.

41. Mrs Perrett also submitted that, given the previous mistakes and, particularly bearing in mind the personal problems being experienced by the book-keepers, it would have been expected that the directors would be keeping a very close eye on the company's VAT returns and making sure that they were accurate.

42. In addition, Mrs Perrett drew our attention to the fact that, even if (as they say) the directors only became aware of the inaccuracies either in September or November 2013, they did not notify HMRC until the imposed compliance visit in February 2014. She invited us to infer from this that the inaccuracies were deliberate and not just mistakes.

43. Another significant factor, according to Mrs Perrett, is the fact that the input tax figures (and the amount of the appellant's purchases) was always correct and consistent with the Sage records. Coupled with the fact that the inaccuracies in relation to the sales figures were always in the appellant's favour, she argued that this was further evidence that the inaccuracies must be deliberate and not merely a mistake.

44. Finally, Mrs Perrett argued that, although the directors might not have felt confident in using Sage themselves, there is no reason why they could not have instructed the book-keeper to prepare the VAT returns using Sage rather than using the manual records. This would have ensured that the sales figures were captured accurately each quarter.

45. We have considered carefully all of the arguments put forward by both parties. We have borne in mind that the burden is on HMRC to prove on the balance of probabilities that the inaccuracies were deliberate. In our view, HMRC has discharged that burden.

46. Our starting point is that, having had a £30,000 VAT bill in May 2011, we would expect the directors to take care to ensure that future VAT returns are accurate. However, the very next VAT return and the following eight VAT returns after that contained the same mistakes.

47. The directors confirmed that they looked at the VAT summaries. These summaries consisted of a single sheet of paper with two columns. The right-hand side detailed purchases and the input tax on those purchases together with the months covered by the return. On the left-hand column, the sales were shown together with the output tax on the sales and the months the sales figures related to. The net amount

of VAT payable (output tax less input tax) was shown at the bottom of the page. It is obvious from even a glance at the summaries that the sales/output tax months, for the most part, bore very little relation to the period for which the VAT return was being submitted, while the months for purchases/input tax was always correct.

48. The understatement in the company's sales over the period in question was just over £1 million. The company's total sales over the relevant period was just under £3 million. The inaccuracies therefore represent on average close to 35% of the company's turnover. In some periods, the figure was closer to 50%.

Although the directors claim that they only looked at the net amount of VAT payable when they reviewed the VAT summaries, we do not think that they could have failed to spot such significant errors.

49. It is apparent that the directors do know how the VAT returns should be correctly completed as they have managed to complete the VAT return for the period ended 09/13 and subsequent VAT returns accurately. This supports our view that it is inherently improbable that the directors would not have noticed the mistakes in the VAT summaries for previous periods.

50. We agree with HMRC that the fact that all of the purchase figures were stated accurately on the VAT return and that all of the mistakes were in the appellant's favour adds further support to the conclusion that the inaccuracies were deliberate rather than careless.

51. Although the directors say that they only became aware of the inaccuracies when alerted to them by their accountant in either September or November 2013, this statement was not supported by the accountant when responding to a specific question from HMRC on this point.

The amount of the penalties

52. HMRC's penalty explanation schedule issued on 23 June 2014 explains how the penalties were calculated and, in particular, how HMRC arrived at the total reduction of 85%.

53. The maximum reduction is 100%. HMRC's practice is to allow a maximum of a 30% reduction for telling HMRC about the inaccuracy. They have allowed 25% in this case on the basis that, although the directors volunteered at the beginning of the meeting on 19 February 2014 that there were sales that had been omitted from the VAT returns, the amounts were not quantified and there was no credible explanation as to why the inaccuracies had occurred.

54. The maximum reduction which HMRC will normally give for helping in the enquiry is 40%. In this case, HMRC has allowed 30% as the appellant did not provide a calculation of the understatement in the tax liability. Instead, HMRC had to work this out for themselves.

55. HMRC did however allow the full 30% reduction which they normally allow for helping HMRC in its enquiries. This was because they were given full access to the information they needed to work out the correct figures.

56. We would agree with the approach that HMRC has taken. Having looked at all of the relevant factors, we do not think that a full 100% reduction would be appropriate. An 85% reduction is in our view correct in this case.

Suspension and special circumstances

57. The appellant was under the impression that HMRC had agreed to suspend the penalties. However, it is clear from the documents we have seen that there were two penalties which were charged. One was for the understatement of the VAT liability which related to the omission of sales figures. The other was for an error in applying fuel scale charges. The penalty explanation schedules are clear that it was the penalty relating to the fuel scale charges which was suspended and not the penalty for the omission of the sales figures.

58. Having found that the inaccuracy relating to the sales figures is a deliberate inaccuracy, it follows that the related penalties cannot be suspended as suspension is only possible if the inaccuracy is careless.

59. We have also looked at whether there are any special circumstances. The appellant has drawn attention to the fact that it is a small business operating in a deprived area of Wales and that its employees are dependent on the jobs which it provides. It has said that, if the penalty is upheld, it will have to cease business. This is partly as a result of the company's customer base having reduced in size during the last six months as a result of Ministry of Defence spending cuts and a reduction in margins.

60. The appellant also relies on the fact that, for the VAT periods from 09/13 onwards, the directors have prepared the VAT returns and that these have all been correct. In addition, all outstanding payments of VAT have been made.

61. However, whilst the appellant's subsequent conduct could perhaps be relevant as to whether the previous inaccuracies are careless or deliberate, it does not, in our view, represent a "special circumstance" which we can legitimately take into account.

62. As far as the company's financial position is concerned, we are prohibited by paragraph 11(2)(a) of schedule 24 to FA 2007 from taking into account as a "special circumstance", the company's ability to pay. The fact that the company might have to cease business if the penalty is upheld is, in reality, another way of saying that the company is not in a position to pay the penalty. Whilst we have every sympathy for the company's predicament and that of its employees, the legislation does not allow us to take this factor into account in our decision.

Our decision

63. For the reasons set out above, we find that the inaccuracies were deliberate rather than careless, that the reduction applied by HMRC is appropriate and that there are no special circumstances which would justify a further reduction.

64. We therefore uphold the penalty as assessed.

65. This document contains full findings of fact and reasons for the decision. Any party dissatisfied with this decision has a right to apply for permission to appeal against it pursuant to Rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. The application must be received by this Tribunal not later than 56 days after this decision is sent to that party. The parties are referred to "Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

ROBIN VOS
TRIBUNAL JUDGE

RELEASE DATE: 9 MARCH 2016